

State Board of Equalization

OPERATIONS MEMO

For Public Release

No : 1141

Date: September 19, 2006

SUBJECT: Escrow Procedures

I. GENERAL

This memo is being issued to standardize some escrow clearance procedures in order to maximize staff efficiency and responsiveness to taxpayer issues during the escrow clearance process.

The escrow clearance process may involve a variety of staff depending on how the request for a clearance is received. In large district offices, requests received by mail or fax will generally be handled by the district office escrow technician. When the taxpayer or the taxpayer's agent personally appears in the office, a tax technician working the counter may be tasked with conducting the escrow clearance process provided all the required information is submitted.

Clearances should not be issued until all of the sales and use tax liability of the seller has been determined and paid, or security is posted in accordance with Revenue and Taxation Code section 6813. The Board must issue either a BOE-471, *Certificate of Payment*, or a BOE-1274, *Notice of Amounts Due and Conditional Release*, when the purchaser of a business or his/her agent makes a written request for a certificate stating that no tax is due (henceforth a "sales tax clearance"). The BOE-471 or BOE-1274 must be issued within 60 days of one of the three following events, whichever event occurs last:

- after the Board receives the purchaser's written request for a sales tax clearance, or
- from the date on which the former owner's records are made available for audit, or
- from the date of the sale of the business or stock of goods.

Many districts have delegated the approval of escrow clearance documents to the following: Business Tax Specialists, Business Taxes Compliance Specialists and Business Taxes Representative, Range C.

II. INTERDISTRICT COOPERATION

If a request for a tax clearance is received in the mail by a district that is not the district of control, the request should be mailed to the district of control immediately. If a request for a tax clearance is received in person in a district that is not the district of control, the escrow technician in the receiving district should insure that all necessary information is included in the request. If all information is present, and if the account appears clear, the escrow technician should inform his/her supervisor, and the escrow technician will contact the district of control's

escrow person, relay the escrow information, and seek approval of the district of control to issue a clearance. If the district of control gives approval to issue the clearance, the receiving district should issue the clearance and send copies of all information to the district of control. However, if all information is not present and/or if more research is required before a clearance can be issued, the receiving district should inform the district of control that an escrow request has been received and forward the escrow request to the district of control. Additionally, a letter will be sent to the escrow agent to notify such agent that their request has been forwarded to “name, address, and phone number” of the district/branch office that is responsible for issuing the clearance.

When other Board offices are involved with the account, e.g., consolidated permits with active sub-locations in other districts, the clearance is to be issued or approved by the district where the account’s master location is assigned. When a consolidated account sells all but one of its sub-locations and an inter-district move is required, the district of control for the account is responsible for transferring the account to the new district.

III. PROCEDURES

The following procedures must be followed when a request for a sales tax clearance is received:

- A. Log the request in the Escrow Log and assign a control number to the account. Indicate the name of the taxpayer, the account number, the date the request was received, and the escrow number. Many times the names of the parties involved in the escrow provided by the escrow company do not match the name(s) of the owner appearing in the board’s records. Therefore, the name(s) of the seller on the escrow documents must be checked carefully against the name(s) of the owner on the seller’s permit. If necessary, a new permit should be issued reflecting the actual ownership and records transferred to the new permit number prior to issuing a clearance or conditional release.
- B. If a request for a clearance comes to the escrow desk and the seller’s account is an active collection case, the escrow technician must notify the collection supervisor via email of the escrow request without delay and continue processing the escrow request. The supervisor will enter information regarding the escrow request into ACMS and forward the email to the responsible collector. Some districts use ACMS to track the escrow using ACMS Special Processing state S-53 and assign the case to the Escrow Technician rather than routing it to the collector.
- C. Prepare an escrow folder (working file) for each escrow account. If an audit is recommended, complete the form BOE-406, *Closeout Worksheet*, and forward it to the audit staff with supporting documentation. The BOE-406 is a convenient way to make sure that all the escrow required documents have been received and its use as a control document is recommended.
- D. If the clearance request is not made by an escrow company or escrow agent, send forms BOE-467, *Notice of Requirements in the Sale of a Business*, and BOE-65, *Notice of Closeout for Seller’s Permit*, to the seller and buyer to obtain any

documents needed to issue the clearance, for example, the bill of sale, copies of sales and use tax returns filed by the taxpayer, copies of canceled check(s), etc. The BOE-65 should be completed with an exact closeout date, if possible. Since all sales up to the last day of business need to be reported on the taxpayer's final tax return, using an estimated closeout date may result in delays in processing the clearance.

- E. In IRIS, search CTS by owner name, fictitious business name (DBA), business address, Social Security number or TIN number (if known) to locate the account number and any related account numbers. Note any liabilities that are due on any accounts held by the seller and, if any liabilities are discovered or generated through investigation, follow the steps outlined in III B above. The CTS search must be recorded in IRIS comments. Any review of an account that is requesting an escrow clearance should consider the possibility of issuing a dual determination for "predecessor's liability", as described in CPPM sections 775.010 and 775.015.
- F. The TPS TP screen (see example screen picture below) is an account summary that provides for a quick review of active account information to determine whether an account has a balance due, is delinquent or revoked, is assigned for audit, etc. The TPS TP screen does not display non-final or unbilled items. This screen should not be used to the exclusion of other pertinent information screens such as those listed below:
 - 1. TAR AI - Is there a liquor license issued to the account? If so, has a "hold" been placed against the transfer of the liquor license? If not, notify the responsible collector. Since TAR AI does not always contain ABC license information, the escrow technician should perform a search of ABC's website or contact ABC directly to determine whether or not an alcoholic beverage license has been issued to the seller.
 - 2. DIF/DA – Check and record any balances due. Notify responsible collector.
 - 3. SEC/IS – Is there an active security deposit? If yes, forward a request to the security desk to apply or refund available security. The Board is required to issue a demand for payment to the financial institution for non-cash security deposits, when a person selling a business requests that a security deposit be applied against an outstanding liability. These funds should be received from the bank prior to being credited in a BOE-1274. If the 60-day time frame is approaching, the BOE-1274 should include the total balance due without showing a credit for the security deposit. An explanation of this action should be provided to the buyer or his agent.
 - 4. DEL/BD – Insure there are no delinquent tax returns.
 - 5. AUD/ME – What is the current audit status (selected, active, pending)?

6. PAY/BA – Have any current payments been received? Record the amount(s) and the cash date(s).
7. REV/FZ – Check and record any prepayments or returns.

TEALE - EXTRA Personal Client

File Edit View Tools Session Options Help

TPSSC1P1 - TPS * Sandbox * Taxpayer Summary 01/26/06
 TPSSC1P1 - TP Taxpayer Profile 08:03

Acct: 100100100 RB : TIN:
 TP: :
 DBA : Start:
 Status:

Active Information

Tax : Del: Revoked:
 Interest: Security Amount:
 Penalty : Prime/Secondary:
 Total : Legal: Appeal:

Assigned for Audit: Last Audit Thru:
 Tax:

Del: Revo: Summary

Go:
 F1=Help, F2=Ntask, F3=Retn, F10=VwReg, F11=Cmnts, F12=Flip, F15=Menu, F24=Asc

EQCPR3N1: Account not found

01/18 04/18
 Connected to host: mvssys5.teale.ca.gov [134.167.32.5] (EQTN1323) [NUM] 8:03 AM

- G. Enter escrow information in IRIS Comments. The subject line should read: ESCROW/SALE OF BUSINESS. Information to be recorded includes:

1. The date the escrow request was received and the 60-day expiration date.
2. The name and address of the escrow company as well as the escrow number.
3. The buyer's name, address and account number (if a permit has been issued to the buyer at this time). Even though issuing a seller's permit to the purchaser is not a prerequisite for the clearance, the purchaser should be in the process of obtaining a permit. If the sales tax clearance is issued and the purchaser still has not applied for a seller's permit, an assignment will be generated to conduct regular follow-ups until the purchaser is registered. A Form BOE-449 (New Permit Required letter) should be sent to the purchaser and a copy retained in the escrow case file. The purchaser should be contacted within two weeks of mailing the BOE-449 to confirm receipt of the form and to establish a date for its return.
4. The address of the business location(s) being sold (including sub- location number(s)).
5. An allocation that shows the purchase price, the value of fixtures and equipment, inventory, goodwill, and other terms of the sale agreement. If an escrow company or legal agent is involved, the allocation will be included in the escrow instructions or the purchase agreement. If a clearance request is received from a

buyer/agent, the bill of sale may or may not include the breakdown of the purchase price. This breakdown must be provided before a clearance can be issued. If this information is not included in the escrow instructions or the sales agreement, the escrow technician must request that it be provided.

6. Any relevant information about the escrow that is provided by the taxpayer. Tax returns received in the district office must be checked for computational errors but should not be written on. A comment that the final return was reviewed for accuracy should be entered.
7. Updated forwarding addresses and phone numbers which should be entered into IRIS as comments. When the escrow is completed and the seller's permit is closed, be sure to update the appropriate IRIS address fields.
8. Verification of the closeout date.
9. Proof of payment for any payments made within 30 days of closing the business. For escrow purposes, payments received in response to the BOE-65 must be made in certified funds or cash. Taxpayers that file and pay by Electronic Funds Transfer (EFT) must continue to make EFT payments. Copies should be sent to the district office for the escrow desk file. If payment is made by other than EFT, then EFT penalties will apply to those payments.
10. If the final tax return or information regarding the seller's final tax liability is not received within 30 days after receiving the clearance request or close-out date, whichever is later and no reply has been received from the seller in response to our mailing the BOE- 65, the seller will be sent form BOE-360, *Final Return Due – Closed-Out Account*. A follow up will be set for 15 days (day 45 from date of the clearance request or close-out date). If the taxpayer does not respond to the BOE-360, action should be taken to establish a liability; however, a notice of determination should not be issued until five days prior to the 60th day. Be aware that when the close-out date falls in the middle of a reporting period, the return is not due until the actual due date of the return. For example, if the seller reports on a quarterly basis and the close-out date is May 15, XXXX, then the return is not due until July 31, XXXX. In this case, the return is not due until after the 60-day period to issue an escrow clearance has expired, provided we received an escrow clearance request prior to June 2. When this occurs, the escrow company, the buyer and the seller should all be put on notice that a tax clearance will not be issued unless all the required documents are received, all delinquencies are cleared, and all amounts owed are paid in full with cash or certified funds within the 60-day period.

- H. If the account is selected for audit, a letter should be sent to the escrow company informing it that the account will be audited. The letter should also advise that if

the purchaser requests to close escrow before the audit is completed, a security deposit (in an amount determined by the District Principal Auditor or assignee) sufficient to cover any liability up to the full purchase price will be required in order to expedite issuing the clearance. Security deposits may be received from a third party (see CPPM 455.060). Pursuant to CPPM Section 410.080, security deposits required to be posted when a business or stock of goods is sold “should be limited to cash type deposits, including Third Party deposits.” Discretion and good judgment should be used at all times when determining the amount of required security. When the audit is completed, a copy of the final audit summary report should be requested from the audit staff in order to make demand on the escrow for any amount or amounts determined to be due.

- I. Progress notes should be periodically entered into IRIS comments regarding returns received, payment for tax on the value of furniture, fixtures and equipment (F&E) sold, updated closeout date, audit progress, etc. Missing requirements should be noted at every follow up stage.
- J. If the taxpayer did not report the sale of F&E on line 2 of its final tax return, a One-Time Miscellaneous Financial Obligation (OTM) must be created for the quarter in which the business was sold and the “revenue” must be established in IRIS (revenue is the taxable measure used to determine the amount the taxpayer owes to the Board). Payments (remittances) that are designated as tax on the sale of F&E and that are remitted separately from the final return are then applied against the revenue. Establishing the revenue is not the same as issuing a Compliance Assessment (CAS). Establishing the revenue (REV DF) for this OTM should be done when payment of the tax on the sale of F&E has been received from the escrow and creating a difference is necessary in order to apply the payment.

On the other hand, a CAS establishes a liability in IRIS on the taxpayer’s account. Once the CAS is reviewed and approved by a supervisor, it is sent to headquarters for billing. If the account is billed prior to receipt of the payment from the escrow, the system has no remittance to apply against the revenue, so the taxpayer receives a Notice of Determination (NOD) that shows a balance due. In order to avoid sending the seller an unintended NOD, a CAS should not be created to establish the tax due on the value of the F&E sold if payment is expected from the escrow company. As stated in the previous paragraph, and using the following procedures, an OTM should be created to establish the revenue for the sale of the F&E when the payment is received from the escrow company:

Creating a One-Time Miscellaneous Financial Obligation

- Enter REV FM at the Go Line.
- Type the Account Number.
- Type “OTM” in the FO Type field.
- Type the Start and End Dates.
- Type the Rev Due Date.

- Type the Pay Due Date.
- Press F9 to Add the FO.
- Press F11 and add Comments.
- To see the newly added FO, go to the REV FZ screen.

For additional assistance in calculating Bradley-Burns Uniform Local Sales and Use Tax and Transactions (sales) and Use Tax when creating a CAS for F&E, refer to CHRD Bulletin 51 (available on e-BOE) for instructions on completing these schedules.

Establishing Revenue for the Sale of F&E

Note: An OTM must exist in order to establishing the revenue for the sale of the F&E.

- Enter REV DF and the Account Number at the Go Line.
- If a Smart Box appears, select the appropriate FO.
- If there is no FO in the Smart Box, Press F3 and type the Account Number and Period Code.
- Type the F&E amount.
- Enter the Source, Basis and Justification.
- Press F18 to Calculate.
- Press F5 to Update.
- Verify the correct tax allocation in REV RE. If it is not correct, enter a "M" in the moreable field (>) next to "Local Tax" in REV RE. This field is used for adjusting a compliance assessment for district tax. Make the necessary adjustments to correct the incorrect tax allocation.

If funds are not received from an escrow company to satisfy the tax due on the sale of F&E, and it has not been reported on the final return, the escrow technician must ensure that a CAS is completed and the taxpayer is billed for the amount due. An OTM must be created in the same manner as mentioned above, although the liability will be established by creating an assessment through the REV DE screen in IRIS.

IV. CLEARANCE FORMS

During the escrow clearance process, the forms listed in the following table should be distributed to the indicated parties and the distribution entered into IRIS comments.

Document Distribution Table

| | | | | |
|--------|---|--|--|--|
| ESCROW | BOE-65 <i>Notice of Closeout for Seller's Permit</i> | | BOE-467 <i>Notice of Requirements in the Sale of a Business</i> | |
| SELLER | BOE-65 <i>Notice of Closeout for Seller's Permit</i> | BOE-467 <i>Notice of Requirements in the Sale of a Business</i> | Pub 74 <i>Closing Out Your Seller's Permit</i> | Reg 1702 <i>Successor's Liability</i> |
| BUYER | BOE-449 <i>Ltr re: Permits Required</i> | BOE-400 <i>Permit Application</i> | BOE-467 <i>Notice of Requirements in the Sale of a Business</i> | Reg 1702 <i>Successor's Liability</i> |

A. BOE-471, Certificate of Payment

Once all supporting documents and payments have been received, input the close-out date in (IRIS) and prepare the form BOE-471 for supervisor (or designee) review and approval. This form is used when all the sales and use tax liability of the seller has been paid to the Board of Equalization. Make four copies of the approved and signed BOE-471. The original and the copies for the buyer and the escrow holder are mailed to the escrow company to distribute. The fourth copy is sent to the HQ Special Procedures Section (CPPM 650.030).

B. BOE-1274, Notice of Amounts Due and Conditional Release

This form may be used as a withhold for an estimated amount or selling price if there is money due from the seller. When all supporting documents have been received and payment is due, input the close-out date into IRIS and prepare the BOE-1274 for supervisory (or designee) review and approval. If approved, make five copies. As with the BOE-471, the original BOE-1274 and the copies for the buyer and the escrow holder should be **mailed to the** escrow company for distribution. The third copy should be retained in the district for three years; ten years for amnesty liabilities; or until the statute for successor billing has expired. The fourth copy should be sent to Taxpayer Records, MIC:36. Once the demand is satisfied, the fifth copy should be forwarded to HQ Special Procedures Section, MIC:55, pursuant to CPPM 650.030 if there is an action necessary by that Section. The seller may not pick up the BOE-1274 because of the balance due on the account. A follow-up with the escrow company to determine the status of the payment needs to be made. If no payment is received after 30 days, telephone the escrow company to determine the status. If necessary, prepare a BOE-86, *Assignment Report*, or BOE 452, *Compliance Activity Report*, and submit to supervisor. If only tax on the sale of F&E is due, process an OTM using the procedures outlined earlier.

Although Sales and Use Tax Law section 6812 allows the Board 60 days to issue a BOE-471 or BOE-1274, if all information is received and verified prior to the expiration

of the 60-day period, the BOE-471 or BOE-1274 should be sent out without further delay.

The clearance documents above, as well as the BOE-406 if one is used, will be routed to Taxpayer Records for inclusion in the taxpayer's file. It is important that the clearance process is completely documented and that the taxpayer is provided with all of the documents that inform them of their rights and obligations in case there are questions or concerns later.

C. Cancellation Letters

In cases where the seller is not forthcoming with documents necessary to timely issue a sales tax clearance, a cancellation letter may be sent to the buyer, the seller, and the escrow company or agent. The letter should identify the information required to complete the clearance process, set a deadline for submission of the required documentation, and make clear that the clearance process will be cancelled if the required information is not made available.

If you have questions regarding these procedures, please contact the Compliance Policy Unit at (916) 445-5167.

V. OBSOLESCENCE

Compliance Policy and Procedures Manual Chapter 6, *Closeouts and Clearances*, is currently under revision. This memo will become obsolete when the new escrow clearance procedures are incorporated into Chapter 6.

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